



Wyoming Lender Alert

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Steven Despain, District Director

Making a Difference for Small Business in Wyoming

Open Account Terms Can Increase Your Sales in Global Markets

By

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The world has become an increasingly competitive market-place. A flood of products from China, technical services from India, competitive financing packages from Asia, and government support for exporters from several countries. How can an American exporter win? An often overlooked option is for U.S. exporters to offer more competitive, open account payment terms, with the additional risk mitigated through credit risk insurance.

Traditionally, there are four main ways to get paid for export sales. From the most conservative to the most risky for the exporter, they are:

- Cash-in-advance
- Letter-of-credit
- Documentary collections
- Open account terms.

Cash-in-advance is pretty straight forward: You are telling your buyer to send you the money, and you will send the goods—safe for you, but a big risk for your buyer! (When you receive the money, you have both the cash and the goods, and your buyer has neither!) So, some buyers may be rather hesitant to jump at this payment option. The risk to you the exporter, however, is basically zero **if** you have the products in inventory and ship them after receiving the funds, or **if** you only begin producing the order **AFTER** you receive the funds, using your buyer's money to finance your working capital needs for the production cycle.

A documentary letter of credit is relatively safe, because it will ensure that

money has been deposited in your buyer's bank and, if you can document that you met the terms and condition of the letter of credit, you will be paid. This instrument has been very effective in reducing the perceived risks between buyers and sellers who might not know one another very well, because they trust their respective banks: a) to not release the funds until there is documentary evidence that the order has been shipped (from the buyer's perspective), and b) to be paid shortly after goods have been shipped (from the seller's perspective).

Documentary collections use the banking system to ensure that goods are paid for (cash against documents) or a promise is made to pay for them (documents against acceptance) before the goods are received. The buyer can only receive the transportation and title documents when one of those conditions is met, helping to assure the exporter that he will be paid before the goods are released. While the banking system does not have enforcement powers (or any responsibility for ensuring payment), this method works well for known, reliable buyers using a developed, transparent banking system, typically in Western industrialized countries.

Open account terms generally are viewed as the most risky method of the payment for international transactions. Do you really know the credit worthiness of your buyer in Brazil or South Korea? Well, you can (and should) conduct standard due diligence by ordering credit reports on overseas buyers, just as you do for domestic buyers. Several companies sell such reports, such as Graydon America, Owens Online, Credit Risk Monitor, and Dun & Bradstreet International. But, once you qualify your buyer for open account terms, commercial and political risks still remain. While commercial risk exists for any buyer, there might well be

additional risks related to your buyer's country that could impact your customer's ability to pay. These political risks will vary widely by country and over time, but they will exist, even when selling to Canada. When you cross the border, your exposure is no longer is in the United States.

Fortunately, there is a well-established way to mitigate these commercial and political risks. Called *credit insurance*, it is a specialized insurance with all the standard insurance features: a policy, a premium, a deductible and a claims process in case of loss. You can get a free quote from special insurance brokers and will not incur any costs until you commit to a policy. Insuring overseas accounts receivable offers U.S. exporters several advantages:

1. You can sleep at night, knowing if there is a default on your foreign accounts receivable, the insurer typically will pay 90-95% of the invoiced amount.
2. You will be able to secure additional orders—and, generally larger orders—than you would by only offering cash-in-advance or letter-of-credit payment options, because your buyers will not have to come up with the money up front (cash-in-advance) or prior to receiving the goods (letter-of-credit).
3. You will be able to borrow against the insured, foreign accounts receivables—unlike uninsured foreign accounts receivables, which lenders typically kick out of any borrowing base. Credit insurance will enhance your ability to secure working capital to support your transactions or ongoing business. Importantly, the U.S. Small Business Administration's Export Working Capital guaranty loan program can be used along with credit insurance to

establish a revolving line of credit (up to \$2 million) to fund your export transactions.

What is the cost? For a small business with less than \$5 million in open account sales to foreign buyers over the past two years, the cost is only 65 cents per \$100, or .65%, of the invoiced amount under the Eximbank small business policy—a pretty small mark-up to secure the three benefits listed above. And, typically this cost can be passed through to the buyer, who would much prefer having open account terms and avoiding the additional costs related to opening a letter-of-credit or paying cash in advance. For companies with more than \$2 million in foreign, open account sales annually, an even less expensive credit insurance policy probably could be obtained from one of the large private insurers such as Coface, FCIA Management, Euler Hermes, or AIG.

So, as you think about how to expand your export business in the coming months, consider offering open account terms to your buyers—which you can do prudently by securing credit insurance on those sales. In a world that is becoming more competitive every day, being able to offer open account terms on an insured basis could very well make the difference in your international sales success.

Why Are 504 Loans of Interest to Banks?

*From Controller of the Currency,
Community Affairs Department
February 2006 Issue*

504 loans are attractive to banks because these loans can retain and attract customers, assist in risk and liquidity management, and provide fee and interest income. The program enables banks to collaborate in a co-lending product that provides long-term financing to small business customers who would not otherwise be able to find the type of financing product that would allow them to preserve capital for long-term growth. (The CDC loan has a fixed interest rate for the term of the loan. The bank loan may have either a fixed or floating rate.) The 504 loan program provides risk management advantages to participating banks, such as limiting their credit exposure to a single customer, providing good collateral coverage for their retained portion of the loan, and facilitating

liquidity management through an active secondary market.

Credit risk is partially mitigated by a low loan-to-value (LTV) ratio, which typically does not exceed 50 percent. Banks' 504 loans are collateralized by real estate or other fixed assets, and most importantly, the exposure on 504 loans is tiered with banks having the first lien position. The CDC loan is subordinate to the banks' first position on the debt. In addition, 504 loans may help a bank manage its lending limits, industry exposure, and liquidity because an active secondary market for 504 first lien loans exists.

Banks can earn fees and interest income on interim loans related to the project.⁷ Separately, a bank providing the permanent 504 loan may also offer a construction loan for projects requiring new construction, rehabilitation, or reconfiguration of an existing structure. These construction loans typically generate origination, documentation, and inspection fees.

Banks also can earn income if they sell the first lien loan in the secondary market and may be able to cross-sell a variety of other financial products and services as the business continues to grow. In addition, banks may purchase 504 loans from originating banks, securitize the loans, and generate income from the retained servicing activities of the portfolio.

As loans of less than \$1 million represent more than 60 percent of the commercial and industrial (C&I) loans made by national community banks, loans to small businesses are likely to form a significant part of their lending business.⁸ SBA 504 loans may help banks with their mission of local economic development by enabling them to assist small businesses to grow and produce jobs.

How Do SBA 504 Loans Work?

*Reaching Customers
From Controller of the Currency,
Community Affairs Department
February 2006 Issue*

There are a variety of ways through which a bank connects a borrower with a 504 loan. The connection mechanism depends on a number of factors, including the condition of the local real estate market, the capacity of CDCs operating in the state, competition among CDCs operating in the state, and the receptiveness of banks to offering 504 loans.

Typically, bank customers looking to purchase either a facility to house the company's operations or heavy equipment for their businesses will discuss financing needs with their bank. Depending on the bank's knowledge of, and comfort with, SBA 504 loans, its staff may either present the 504 loan as one financing option or refer the customer to a CDC that would explain a 504 loan to the customer.

In some areas of the country, borrowers are referred to banks by commercial real estate brokers who advertise particular properties as potentially qualifying for 504 financing. In these areas, a competitive market for 504 loans exists among banks. Borrowers may also be referred either to banks or CDCs by local professionals with whom they do business, including accountants and lawyers.

Banks that have dedicated government lending departments generally undertake specialized marketing of the 504 program. Some of these banks have sales personnel dedicated to SBA products and are engaged in active marketing of 504 loans to commercial customers as well as CDCs, commercial real estate brokers, and other professionals, including professional associations, where potential borrowers may have contacts. Other banks have SBA divisions that serve as advisors to relationship managers throughout the bank and are brought in to provide SBA product expertise if the bank's in-house products do not fit a particular project. Generally, banks with specialized SBA departments obtain about 80 to 90 percent of their 504 borrowers from their marketing and outreach or from referrals from bank relationship managers, with the remainder referred by CDCs.

Many community banks that engage in a limited number of 504 deals annually typically benefit from the outreach and marketing conducted by CDCs to promote 504 loans. When these banks have a customer who would benefit from a 504 loan, the bank may contact a CDC operating in the bank's state to assist it in describing the 504 product to the customer. CDCs often will conduct joint marketing calls with these banks on potential borrowers, serving as the product expert in these discussions. Smaller

banks, in particular, may value the role of CDCs in enabling the bank to provide SBA products that the bank might not otherwise be able to offer.

A bank may also use the secondary market purchases of 504 loans to build its 504 portfolio. For example, one larger bank partners with community banks across the country that refer customers who would benefit from 504 loans. In these transactions, the larger bank makes the 504 loan to the borrower and pays the community bank a placement fee.

Tips for Business Success Dealing Effectively with Lenders

How to deal effectively with lenders is a very important part of the business process.

Lenders are a fountain of knowledge on how to run a successful business as they see many business management teams work through issues. Ask their help with your problems, they can be a big help.

Lenders judge you on your ability to work out of problems. When you bring them into situations early and tell them what is happening, they begin to trust you and a relationship starts forming. Having a great relationship with your lender has many re-wards. If they trust you they will give you a better interest rate and require fewer covenants.

Lenders do not like surprises. Bringing them into your business concerns early, allows them to watch the solution play out. An old wise saying is "don't go to your lender when you need money". This is true. You need to go to your lender before you need the money to build a relationship. You wouldn't give money to a stranger if he asked you for a loan because you wouldn't know if you would get the money back. If you got to know and trust this person, you might consider a loan because you would then feel this person worthy and dependable. This is what your lender wants to feel before he loans you money. Some businesses do not want to give their lenders any more information than is absolutely necessary.

If this is the case, the lender feels the strain and believes there is something that the business person is holding

back. Always give your lender more than they want and let them pick out what they find useful and discard the rest.

2006 Small Business Week Award Winners For Wyoming

Small Business Person of the Year, Mumtaz Khan, Prime Lodging, Inc., Gillette, nominated by Diane Johnston, WIDC/ Frontier CDC;

Financial Services Champion of the Year, Andrea McCall Presse, Laramie, nominated by Rosemary Bratton, WWBC;

Home-Based Business Champion of the Year, Meadow Maid Foods, Mike and Cindy Ridenour, Yoder, nominated by Arlene Soto, WSBDC;

Minority Small Business Champion of the Year, Nora Lyons, Cheyenne, nominated by Susan Carter, WY Business Consultants, Inc.;

SBA Young Entrepreneur of the Year, Patrick Zimmerer, Table Mountain Vineyards, LLC, Huntley, nominated by Mindy Petersen, Goshen County Chamber;

Small Business Journalist of the Year, MJ Clark, Lander, nominated by Margie Rowell;

Veteran Small Business Champion of the Year, John Karabetsos, Cheyenne, nominated by Joe C. Perkins and Terry Higginbotham;

Women in Business Champion of the Year, Robbi Welch, Powell, nominated by Amy Lea, WWBC;

SBA Family-Owned Small Business of the Year, Glenda Santoni and Beth Kudlak, Casper, The Plant Peddlers, nominated by Dianna Wallace, First Interstate Bank, Casper.

SBA's SUB-Net Database

Are you a small business owner looking for sub-contracting opportunities but are not sure how to locate these opportunities? The U.S. Small Business Administration has the answer to your dilemma. SUB-Net, the Agency's sub-contracting database, is the place to go to locate subcontracting opportunities with prime contractors. By law prime contractors with awards of \$500,000 for non-construction and \$1,000,000 with awards for construction related contracts, are required to post subcontracting

opportunities for small businesses in SUB-Net.

Prime contractors use SUB-Net to post subcontracting opportunities, which may or may not be reserved for small business, and they may include either solicitations or other notices, i.e., notices of sources sought for teaming partners and subcontractors on future contracts. Small business owners may review this website to identify opportunities in their areas of expertise, and it is an excellent website for veteran business owners to identify and submit bids on subcontracting opportunities with prime contractors.

The website was designed primarily as a place for large businesses to post solicitation and notices, but it also is used by federal agencies, state and local governments, non-profit organizations, colleges and universities and even foreign governments for the same purpose.

The new website has shifted the traditional marketing strategy from the shotgun approach to one that is more focused and sophisticated. Instead of marketing blindly to hundreds of prime contractors, with no certainty that any given company has a need for their product or service, small businesses can now use their limited resources to identify concrete, tangible opportunities to then bid on.

UPCOMING EVENTS

Apr 5 – Women's Roundtable
Casper and Dubois

Apr 6 – Women's Roundtable
Jackson

Apr 9-15 – Small Business Week

Apr 13 – Women's Roundtable
Laramie and Worland

Apr 18 – Women's Roundtable
Cody

Apr 20 – Women's Roundtable
Powell

Apr 27 – Business Expo – Casper
Events Center

GOVERNOR'S PROCLAMATION



WHEREAS, America's economy is the most prosperous in the world and the small business sector is one of its great strengths. During Small Business Week, we honor small business owners and workers, and we reaffirm our commitment to keeping America the best place in the world to do business; and

WHEREAS, our economy is strong and growing stronger. More Americans are working today than ever before. The unemployment rate is lower than the average rate of the 1970's, 1980's, and 1990's. Homeownership is at a record high. Family incomes are rising. Small businesses are at the heart of this growth, creating most new private-sector jobs in our economy and helping our citizens succeed; and

WHEREAS, Small businesses make up 96.6 percent of all Wyoming employees and create more than 50 percent of American non-farm private gross domestic (GDP); and

WHEREAS, the 56,740 small businesses in Wyoming are located in every community and neighborhood and employ 69.3 percent of Wyoming's non-farm private sector workers, and

WHEREAS, Wyoming saw an estimated 2,519 new small firms with employees start-up in the last year; and

WHEREAS, there are approximately 2,500 minority-owned businesses and 12,946 women-owned businesses in Wyoming and almost all of them are small businesses; and

WHEREAS, as small business owners and employees add to the vitality of our economy, they also inspire others to realize the full promise of our Nation. I join all Americans in celebrating the entrepreneurial spirit and hard work of our small business owners and employees.

NOW, THEREFORE, I, DAVE FREUDENTHAL, GOVERNOR, of the State of Wyoming do hereby proclaim April 9 through April 15, 2006, as

SMALL BUSINESS WEEK.

in Wyoming. I call upon all citizens to observe this week with appropriate ceremonies, activities, and programs that celebrate the achievements of small business owners and their employees and encourage and foster the development of new small businesses.

IN WITNESS WHEREOF, I have hereunto set my hand and caused the Executive Seal of the Governor of Wyoming to be affixed this 7 day of March, 2006.



Dave Freudenthal
Governor